(23)

IN THE

Supreme Court

OF THE

United States

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OCTOBER TERM, 1941

NO. 231

HAWAIIAN GAS PRODUCTS, LIMITED,
a corporation,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI

To the United States Circuit Court of Appeals
For the Ninth Circuit

and

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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HAWAIIAN GAS PRODUCTS, LIMITED,
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COMMISSIONER OF INTERNAL REVENUE,
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PETITION FOR WRIT OF CERTIORARI

To the United States Circuit Court of Appeals
For the Ninth Circuit.

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

The petition of HAWAIIAN GAS PRODUCTS, LIMITED, a Hawaiian corporation (hereinafter sometimes called the Petitioner) for a Writ of Certiorari to

the United States Circuit Court of Appeals for the Ninth Circuit, respectfully shows as follows:

I.

SUMMARY STATEMENT OF THE MATTER INVOLVED

This case involves the determination of Petitioner's income tax for the calendar year 1937. The facts of the case were stipulated (Record pp. 15-18) and may be briefly recapitulated as follows:

In 1933 the Petitioner, having its principal place of business in Honolulu, Territory of Hawaii, acquired certain real estate in the Territory of Hawaii which had an adjusted cost basis in its hands in 1937 of $44,979.48. November 2, 1937 the Territory of Hawaii filed an action in the Territorial Courts to condemn, in eminent domain proceedings, among other parcels of land, the above mentioned real estate belonging to Petitioner. The Petitioner filed an answer in that action alleging that it did not wish to sell the property in question but recognized the power and capacity of the Territory of Hawaii to take the real estate under eminent domain. Judgment of condemnation was entered December 1, 1937, which ordered the real estate condemned and payment of damages to Petitioner in the sum of $32,500., which sum represented the value of the land as of the date of condemnation. The said sum was paid to, and received by Petitioner in 1937. The transaction resulted in a loss to Petitioner in said year in the amount of $12,479.48.

The Respondent determined a deficiency in income tax of Petitioner for 1937 in the amount of $5,903.56 upon the theory that the loss in question was a capital loss and therefore subject to the limitations of Section 117(d) of the Revenue Act of 1936. (Appendix p. 1)

Petitioner duly perfected an appeal from this determination to the United States Board of Tax Appeals. The United States Board of Tax Appeals affirmed the determination of the respondent by its decision entered February 18, 1941 (Record pp. 22-23). The Board, in its opinion, reached this conclusion upon the ground that "there is no substantial difference between a loss sustained upon the foreclosure sale of mortgaged property and a loss sustained as a result of a condemnation and taking of property by the Territory of Hawaii" (Record p. 22). Having found that there was no substantial difference between the two types of loss the Board relied upon the opinions of this Court in the cases of *Helvering* v. *Hammel,* 311 U. S. 504, and *Electro-Chemical & Engraving Co.* v. *Commissioner,* 311 U. S. 513, both of which cases held that losses sustained on mortgage foreclosures were capital losses.

Petitioner duly perfected its appeal from the decision of the United States Board of Tax Appeals to the United States Circuit Court of Appeals for the Ninth Circuit. That court, on February 20, 1942, entered its judgment affirming the said decision of the United States Board of Tax Appeals (Record pp. 40-51). The United States Circuit Court of Appeals for the Ninth Circuit in its

opinion (Record pp. 36-40) held that an eminent domain proceeding amounted to a "sale" within the intendment of Section 117(d) of the Revenue Act of 1936. In said opinion no mention was made or consideration given to the case of *Helvering* v. *William Flaccus Oak Leather Co.*, 313 U. S. 247, which case it had been urged by the petitioner, required a reversal of the decision of the United States Board of Tax Appeals.

This case requires the determination of whether said loss may be deducted by Petitioner in full as an ordinary business loss under Section 23(f) of the Revenue Act of 1936 (Appendix p. 1) or whether said loss was a capital loss and thus subject to the limitations provided in Section 117(d) of said Revenue Act. If said loss was a capital loss only $2,000. of said loss may be deducted. If the said condemnation did not constitute a "sale or exchange" within the meaning of those words as used in Section 117(d) of the Revenue Act of 1936 then the loss is an ordinary business loss and may be deducted in full. On the other hand, if such condemnation did constitute a "sale or exchange" within the meaning of those words the loss was a capital loss and subject to the limitations provided in said Section 117(d) of said Act.

II.

REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT

1. The United States Circuit Court of Appeals for the Ninth Circuit in this case has decided an important question of Federal law which has not been but should be settled by this Court.

2. The United States Circuit Court of Appeals for the Ninth Circuit in this case has decided an important question of Federal law in a manner which is untenable.

3. The United States Circuit Court of Appeals for the Ninth Circuit in this case decided a Federal question in a way probably in conflict with *Helvering* v. *William Flaccus Oak Leather Co.*, 313 U. S. 247.

WHEREFORE, your Petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the United States Circuit Court of Appeals for the Ninth Circuit commanding that court to certify and send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and proceedings in the case numbered and entitled on its docket No. 9833, *Hawaiian Gas Products, Limited, a corporation, Petitioner* v. *Commissioner of Internal Revenue, Respondent*, and that the judgment of the said United States Circuit Court of Appeals for the Ninth Circuit

may be reversed by this Honorable Court, and that your Petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just.

DATED: Honolulu, Territory of Hawaii, June 16, 1942.

Respectfully submitted,

HAWAIIAN GAS PRODUCTS, LIMITED,
a corporation,

By—ROBBINS BATTELL ANDERSON,
Attorney for Petitioner

HEATON LUSE WRENN,
of Counsel.

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OCTOBER TERM, 1941

NO.

HAWAIIAN GAS PRODUCTS, LIMITED,
a corporation,
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v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

I.

THE OPINIONS OF THE BOARD AND COURT BELOW

The opinion of the United States Board of Tax Appeals is dated February 18, 1941 and has Docket No. 99806 (Record pp. 19-22). The opinion in the United States

Circuit Court of Appeals for the Ninth Circuit is dated February 20, 1942 and has Docket No. 9833 (Record pp. 36-40).

II.

JURISDICTION

(a) This Court has jurisdiction by virtue of the provisions of Section 240(a) Judicial Code, as amended by Act of Congress of February 13, 1925 (U. S. Code, Title 28, Sec. 347).

(b) The United States Circuit Court of Appeals for the Ninth Circuit entered the judgment of which review is here sought, on February 20, 1942 (Record pp. 40-41). An order extending time within which to file a petition for certiorari in this matter to and including July 18, 1942 was made and filed April 28, 1942.

(c) This case involves the applicability of Section 23(f) of the Revenue Act of 1936 (49 Stat. 1648, 1659) (Appendix p. 1) and Section 117(d) of said Act (49 Stat. 1692) (Appendix p. 1) to a loss sustained by the petitioner as the result of condemnation of certain of its real property by the Territory of Hawaii (Record pp. 37-38.)

III.

STATEMENT OF THE CASE

A full statement of the case has been given under heading I in the petition for certiorari, and for the sake of brevity is not repeated.

IV.

SPECIFICATION OF ERRORS

1. The United States Circuit Court of Appeals for the Ninth Circuit erred in making and entering its judgment, dated Febuary 20, 1942, affirming the decision of the United States Board of Tax Appeals, dated February 18, 1941, Docket No. 99806.

2. The United States Circuit Court of Appeals for the Ninth Circuit erred in finding and holding that condemnation by the Territory of Hawaii of real property of petitioner during the year 1937 amounted to a "sale" of property within the intendment of Section 117 (d) of the Revenue Act of 1936.

V.

SUMMARY OF ARGUMENT

A condemnation of real property is not a "sale" thereof within the meaning of the word as used in Section 117(d) of the Revenue Act of 1936. The word "sale" as used in that Act is to be given its ordinary meaning. Condemnation proceedings are not ordinarily deemed or termed a sale. A sale is ordinarily defined as a voluntary transfer of title to property for a consideration fixed by agreement of buyer and seller. A condemnation of property is a taking thereof which results in the extinguishment of the individual owner's rights and the vesting of a new title in the sovereign with an award of compensation or damages to the former owner judicially determined. The

holding in this case by the United States Circuit Court of Appeals for the Ninth Circuit is to the effect that a condemnation of property is a sale within the intendment of Section 117(d) of the Revenue Act of 1936. This is contrary to the principles established by this Court in *Helvering* v. *William Flaccus Oak Leather Co.,* 313 U. S. 247. The judgment of the United States Circuit Court of Appeals for the Ninth Circuit should therefore be reversed.

A CONDEMNATION OF REAL PROPERTY IS NOT A "SALE" THEREOF WITHIN THE MEANING OF THE WORD AS USED IN SECTION 117(d) OF THE REVENUE ACT OF 1936.

The word "sale" as used in Section 117(d) of the Revenue Act of 1936 is to be given its ordinary meaning. In speaking of the word as used in the corresponding section of the Revenue Act of 1934 this Court, in the case of *Helvering* v. *Willam Flaccus Oak Leather Co.,* 313 U. S. 247, at 249 said:

> "Generally speaking, the language in the Revenue Act, just as in any statute, is to be given its *ordinary meaning,* and the words 'sale' and 'exchange' are not to be read any differently." (Italics ours)

Similarly, in *Helvering* v. *Hammel,* 311 U. S. 504, in speaking of the word "sale" as used in the Revenue Act of 1934, this Court said at pages 510-511:

> "We can find no basis in the language of the Act, its purpose or its legislative history, for saying that losses from *sales* of capital assets under the 1934 Act, more than its predecessors, were to be treated any differently whether they resulted from forced sales

> or voluntary sales. True, courts in the interpretation of a statute have some scope for adopting a *restricted* rather than a *literal or usual meaning of its words* where acceptance of that meaning would lead to absurd results, *United States* v. *Katz,* 271 U. S. 354, 362, or would thwart the obvious purpose of the statute, *Haggar Co.,* v. *Helvering,* 308 U. S. 389. But courts are not free to reject that meaning where no such consequences follow and where, as here, it appears to be consonant with the purposes of the Act as declared by Congress and plainly disclosed by its structure." (Italics ours)

What then is the ordinary meaning of the word "sale"? A sale is ordinarily defined as a voluntary transfer of the title to property for a monetary consideration the amount of which is reached by agreement between buyer and seller.

> *United States* v. *San Francisco,* 23 Fed. Supp. 40;
> *Ratigan* v. *United States,* 88 Fed. (2) 919, at 921;
> *Matteis* v. *United States,* 57 Fed. (2) 999, at 1001.

The Circuit Court of Appeals held that a condemnation of property was a transfer of the same from an individual to a sovereign for a fixed price or consideration. The only difference between a condemnation and an ordinary sale, found by the court, was that it was not a voluntary transaction. This difference, it felt, was unimportant, however, in view of the decision in *Commissioner* v. *Coggan,* 119 Fed. (2) 504, where it was said that, under the authority of *Helvering* v. *Hammel,* supra, and *Electro-Chemical & Engraving Co.* v. *Commissioner,* 311 U. S. 513, the sale need not be by voluntary action of the taxpayer in order to be a "sale or exchange" within the meaning of Section

117. This reasoning of the Circuit Court of Appeals is not sound, however, for although the necessity of voluntary action by the *taxpayer* at the time of the sale is excluded voluntary action by the parties to the sale itself was not excluded. In other words, at a foreclosure sale we do have a seller and buyer acting voluntarily. It so happens the person acting as seller is not the taxpayer. Nevertheless the transaction itself is a sale and customarily and traditionally referred to as such, and it therefore satisfies the statutory definition. One factor which was not expressly mentioned in the *Hammel* and *Electro-Chemical* cases was the fact that the taxpayer-mortgagor had voluntarily, by making the mortgage in the first instance, put himself in the position where a subsequent sale of the property might be made which would not require voluntary action on his part.

The court below asserted that a condemnation was a *transfer* of property for a consideration and therefore a sale. In reaching this conclusion the court gave no consideration to the case of *Duckett & Co.* v. *United States,* 266 U. S. 149 at 151, where it was stated that the accurate view of a condemnation proceeding is that it is a proceeding *in rem* which extinguishes former rights and founds a new title. A condemnation proceeding must therefore be characterized as a *taking* rather than as a *sale.*

Petitioner contended before the Circuit Court of Appeals that a condemnation was not a sale in that there is no transfer of property as a result of eminent domain proceedings but an extinguishment of the individual's title

and the founding of a new title in the sovereign. The Court of Appeals in its opinion stated that this argument may be carried further with the assertion that the result of the condemnation proceeding is a taking and not a sale; that the fixed sum of money passing from the sovereign to the original owner is not consideration but damages (Record p. 39). The Circuit Court of Appeals held that these premises were not controlling for four reasons: First, that the sovereign can get no greater title than that held by the former owner; second, that that which passes from the sovereign to the individual owner as payment is spoken of by the Revised Laws of Hawaii, 1935, Sections 50 to 70, as "compensation or damages" so it is there implied that the payment operates as consideration as well as damages; third, that as a basis for the judgment the compensation is usually arrived at by ascertaining the market value of the property condemned; and fourth, that there is respectable authority to the effect that a proceeding to condemn is in substance a proceeding to compel a sale by the owner of the property.

We submit that each of the reasons advanced by the Circuit Court of Appeals is untenable. With respect to the first reason, that the sovereign can get no greater title than that held by the former owner, the court cites *Bethany Presbyterian Church* v. *City of Seattle,* 154 Wash. 529, at 533. Such an assertion is unsound and not in accord with the law of Hawaii. The action to condemn is *in rem* and the final order to condemn creates a new and unassailable title which is vested in the sovereign. (Sections

59 and 66, Revised Laws of Hawaii, 1935, as amended by Session Laws of 1937. (See Appendix, pp. 1-2). This reason is also untenable in view of the statements of this Court in *Duckett & Co.* v. *United States,* supra. The second reason advanced by the court, to the effect that the reference in the Hawaiian statutes to "compensation or damages" implies that the payment operates as consideration as well as damages, is frivolous. There is nothing whatever in any of the Hawaiian statutes referred to which implies that the compensation or damages are consideration in the sense that a sale has been consummated by the condemnation proceeding. With respect to the third reason offered by the court, we submit that no inconsistency exists between the concept that a condemnation is a taking and the fact that damages are fixed by ascertaining the market value of the property condemned. This seems too clear to require further comment. The final reason offered by the court to the effect that there is respectable authority to the effect that a condemnation is a proceeding to compel a sale is not entitled to any weight in the determination of this case. In the first place the decision in *Duckett & Co.* v. *United States,* supra, is not only more respectable authority than that cited by the lower court but should be controlling with respect to the matter. In addition to that there is the unescapable fact that the Hawaiian statutes with respect to condemnation, which are set forth in the Appendix, do not provide for a forced sale but, as previously pointed out, provide for an *in rem* proceeding by which the rights of all persons

entitled or claiming to be entitled to any particular piece of property are extinguished and a new title "vested" in the sovereign.

It is to be noted in this connection that condemnation of property is characterized by Section 112(f) of the Revenue Act of 1936 as an "involuntary conversion". In *Helvering* v. *William Flaccus Oak Leather Co.*, supra, this Court said at page 250:

> "We can find nothing in this language or in other sections of the Act which indicates, either expressly or by implication, that Congress intended to classify as 'sales or exchanges' the involuntary conversions enumerated in § 112(f)."

In this case the taxpayer's plant was destroyed by fire during the year 1935. Later that year it received compensation from an insurance company for the loss of the plant. The plant had been fully depreciated for income tax purposes prior to 1935 and no part of the insurance proceeds was used to acquire other property similar to that destroyed. This resulted in a taxable gain to the taxpayer and the issue in the case was as to whether the gain was an ordinary gain or a capital gain. This issue reduced itself to the single question of whether the amount the taxpayer received from the insurance company derived from the "sale or exchange" of a capital asset. This Court held that the demolition of the property and subsequent compensation for its loss by an insurance company did not constitute a "sale" within the meaning of the word as used in Section 117(d) of the Revenue Act of 1934. This Court stated that such a pair of events was plainly not a "sale" in the ordinary meaning of the word.

In this case the taxpayer contended that the inference from this juxtaposition of the above sections of the Revenue Act of 1934 was that all the involuntary conversions mentioned in Section 112(f) were characterized and intended by Congress to be considered as "sales or exchanges". The opinion of this Court in this connection is as follows:

> "The inference, drawn from the juxtaposition and cross referencing of these three sections, that the involuntary conversion of respondent's property is thus implicitly characterized as a sale or exchange ignores the fact that in the same Act Congress has chosen a particular method for classifying as sales or exchanges transactions which would not ordinarily be described by one of those terms. Thus § 115(c) provides: 'Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock.'
>
> "Sec. 117(e) provides: 'For the purposes of this title gains or losses from short sales of property shall be considered as gains or losses from sales or exchanges of capital assets; and gains or losses attributable to the failure to exercise privileges or options to buy or sell property shall be considered as gains or losses from sales or exchanges of capital assets held for one year or less.' See H. Rep. No. 704, 73d Cong., 2d Sess., p. 31; H. Rep. No. 1385, 73d Cong., 2d Sess., p. 23. Section 117(f) provides: 'For the purposes of this title, amounts received by the holder upon the retirement of bonds, debentures, notes or certificates or other evidences of indebtedness issued by any corporation . . . with interest coupons or in registered form, shall be considered as amounts received in

exchange therefor.' See *McClain* v. *Commissioner,* 311 U. S. 527; *Fairbanks* v. *United States,* supra; H. Rep. No. 704, 73d Cong., 2d Sess., p. 31.

These sections demonstrate that Congress has expressly specified the ambiguous transactions which are to be regarded as sales or exchanges for income tax purposes. They are convincing evidence that the involuntary conversion of respondent's property, which bears far less resemblance to a sale or exchange than the transactions embraced in § § 115(c), 117(e), and 117(f), is not to be placed in one or the other of those categories by implication. The prompt withdrawal of Article 113(a) (9) (1) of Treasury Regulations No. 86 (see T. D. 4698, XV-2 Cum. Bull. 159) indicates that the administrators charged with the enforcement of § 112(f) reached a similar conclusion. Compare *Burnet* v. *Chicago Portrait Co.,* 285 U. S. 1, 16."

It might be argued that in the *Flaccus* case that this Court did not reach the conclusion that the involuntary conversions listed in Section 112(f) were not intended by Congress to be considered as sales or exchanges, but merely meant to negative the argument of the taxpayer in that case to the effect that the mere listing of a transaction in Section 112(f) as an involuntary conversion impliedly characterized it as a sale or exchange. However, if we examine the reference made by this Court with respect to the withdrawal of Section 113(a) (9)-1 of Treasury Regulations No. 86 (Appendix pp. 2-3) it is at once apparent that the Court had in mind and meant to say that the involuntary conversions listed in Section 112(f) were not sales or exchanges. Said Article 113(a) (9)-1 of Treasury Regulations No. 86 (Appendix pp. 2-3) deals with

"property acquired as a result of involuntary conversion". After illustrating the manner in which a taxable gain would arise through acquiring property as a result of an involuntary conversion the Regulation stated: "As to the amount of such gain to be taken into account in computing net income see Sec. 117". The quoted statement was shortly withdrawn from said Article by T. D. 4698, XV-2 Cum. Bull. 159. This indicates a conclusion of the Treasury Department that the acquisition of property as a result of an involuntary conversion would not be subject to the limitations of Section 117 and the Court in its quoted statement above clearly shows that it agrees with such conclusion.

Helvering v. *William Flaccus Oak Leather Co.*, supra, presents on its facts a close analogy to the present case. In the *Flaccus* case the property of the taxpayer was demolished by the action of an external force and he received compensation for his loss. Similarly, in this case the rights of petitioner in the property involved were extinguished by the action of the sovereign and petitioner received compensation for its loss. In addition to the close analogy, which in itself should be controlling here, the Court went further, as we have pointed out, and clearly indicated that the involuntary conversions listed in Section 112(f) were not to be considered as sales or exchanges within the intendment of Section 117(d). This Court also reasoned from the special designation of the Revenue Act of 1934 (Sections 115(c), 117(e), and 117(f)) of certain ambiguous transactions (liquidation, distributions, short

sales, failure to exercise options and retirement of bonds) as "sales or exchanges" that the "involuntary conversions" designated in Section 112(f) (conversion of property by destructions, theft, seizure or condemnation) were not intended by Congress to be regarded as "sales" for income tax purposes. This was a considered determination which was adopted by the Court in reaching its final decision.

We therefore submit that the United States Circuit Court of Appeals for the Ninth Circuit decided this case in a way probably in conflict with the decision of this Court in *Helvering* v. *William Flaccus Oak Leather Co.*, supra.

CONCLUSION

It is therefore respectfully submitted that this case is one calling for the exercise by this Court of its supervisory powers in order that an important question of Federal law be finally determined and settled by this Court, and that the decision of the United States Circuit Court of Appeals for the Ninth Circuit, which is untenable and probably in conflict with the decision of this Court in *Helvering* v. *William Flaccus Oak Leather Co.*, supra, be reversed and that to such an end a Writ of Certiorari should be granted and this Court should review the decision of the United States Circuit Court of Appeals for the Ninth Circuit and finally reverse it.

DATED: Honolulu, T. H., June 16, 1942.

Respectfully submitted,

By—ROBBINS BATTELL ANDERSON,
Attorney for Petitioner.

HEATON LUSE WRENN,
of Counsel.

APPENDIX

Internal Revenue Act of 1936

Sec. 23(f) Losses by Corporations.—In the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.

Sec. 117(d) Limitation on Capital Losses.—Losses from sales or exchanges of capital assets shall be allowed only to the extent of $2,000 plus the gains from such sales or exchanges. If a bank or trust company incorporated under the laws of the United States or of any State or Territory, a substantial part of whose business is the receipt of deposits, sells any bond, debenture, note, or certificate or other evidence of indebtedness issued by any corporation (including one issued by a government or political subdivision thereof), with interest coupons or in registered form, any loss resulting from such sale (except such portion of the loss as does not exceed the amount, if any, by which the adjusted basis of such instrument exceeds the par or face value thereof) shall not be subject to the foregoing limitation and shall not be included in determining the applicability of such limitation to other losses.

Revised Laws of Hawaii 1935, as amended by Session Laws of 1937

Sec. 59. Petition, defendants, different properties in one action. Actions under and by virtue of this chapter, must be commenced by filing a petition and issuing a summons thereon. All persons who are owners or claimants of the property sought to be condemned must be joined as defendants; provided, however, that in case the owner or claimant is unknown to plaintiff, it shall be sufficient if the petition includes a statement of that fact, and such defendant

may be joined in the petition under a fictitious name. The petition must also contain a statement of the use to which the land sought to be condemned is to be put, a description of each and every piece of land sought to be condemned, and whether the same includes the whole or only a part of an entire tract or parcel. A map must accompany the complaint which shall correctly delineate the land sought to be condemned and its location. All property necessary for any public use may be united in one action. In all proceedings under this chapter the court shall have power at any stage of the proceeding to allow amendments in form or substance in any petition, citation, summons, process, answer, motion, order, verdict, judgment or other proceeding, including amendment in the description of the lands sought to be condemned, whenever such amendment will not impair the substantial rights of any party in interest.

Sec. 66. Final order of condemnation. When all payments required by the final judgment have been made, the court shall make a final order of condemnation, which must describe the property condemned and the purposes of such condemnation, a certified copy of which must be filed and recorded in the office of the registrar of conveyances; and thereupon the property described shall vest in the plaintiff.

Treasury Regulations No. 86

ART. 113(a) (9)-1. Property acquired as a result of involuntary conversion.—*The provisions of section 113(a) (9) may be illustrated by the following example:*

Example: A vessel purchased by A in 1926 for $100,000 is destroyed in 1934 and A receives insurance in the amount of $200,000. Disregarding, for the purpose of this example, the adjustment for depreciation, if A invests $150,000 in a new vessel,

taxable gain to the extent of $50,000 would be recognized. *As to the amount of such gain to be taken into account in computing net income, see section 117.* The basis of the new vessel is $100,000; that is, the cost of the old vessel ($100,000) minus the money received by the taxpayer which was not expended in the acquisition of the new vessel ($50,000) plus the amount of gain recognized upon the conversion ($50,000). (Italics ours)

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In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 231

HAWAIIAN GAS PRODUCTS, LIMITED, A CORPORATION, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 19–22) is reported at 43 B. T. A. 655. The opinion of the United States Circuit Court of Appeals for the Ninth Circuit (R. 36–40) is reported at 126 F. (2d) 4.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on February 20, 1942 (R. 41). An

order extending the time within which to file a petition for certiorari to July 18, 1942, was entered on April 28, 1942. The petition for writ of certiorari was filed on July 14, 1942. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether a loss sustained as the result of the transfer of land by virtue of a condemnation proceeding was an ordinary loss deductible in full under Section 23 (f) of the Revenue Act of 1936, or a capital loss resulting from a sale or exchange of a capital asset, subject to the limitation provided in Section 117 (d).

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1936, c. 690, 49 Stat. 1648:

> SEC. 23. DEDUCTIONS FROM GROSS INCOME.—In computing net income there shall be allowed as deductions:
>
> * * * * *
>
> (f) *Losses by corporations.*—In the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.
>
> * * * * *
>
> (j) *Capital losses.*—Losses from sales or exchanges of capital assets shall be allowed

only to the extent provided in section 117 (d).

* * * * *

SEC. 112. RECOGNITION OF GAIN OR LOSS.

* * * * *

(f) *Involuntary conversions.*—If property (as a result of its destruction in whole or in part, theft or seizure, or an exercise of the power of requisition or condemnation, or the threat or imminence thereof) is cumpulsorily or involuntarily converted into property similar or related in service or use to the property so converted, or into money which is forthwith in good faith, under regulations prescribed by the Commissioner with the approval of the Secretary, expended in the acquisition of other property similar or related in service or use to the property so converted, or in the acquisition of control of a corporation owning such other property, or in the establishment of a replacement fund, no gain or loss shall be recognized. If any part of the money is not so expended, the gain, if any, shall be recognized, but in an amount not in excess of the money which is not so expended.

* * * * *

SEC. 117. CAPITAL GAINS AND LOSSES.

* * * * *

(d) *Limitation on capital losses.*—Losses from sales or exchanges of capital assets shall be allowed only to the extent of $2,000 plus the gains from such sales or exchanges. * * *

* * * * *

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

> ART. 117–2. *Limitations on capital gains and capital losses.*— * * *
>
> * * * * * *
>
> Section 117 (d) provides a limitation on deductions for capital losses affecting all taxpayers including corporations, that is, losses from sales or exchanges of capital assets shall be allowed as deductions only to the extent of $2,000 plus the gains from such sales and exchanges. * * *
>
> * * * * * *

STATEMENT

In 1937 petitioner, a Hawaiian corporation, held certain real estate in the Territory of Hawaii which had an adjusted cost basis of $44,979.48 (R. 19). On November 2, 1937, the Territory of Hawaii instituted an action in a Hawaiian court to acquire this property by eminent domain. Petitioner filed an answer putting the Territory of Hawaii to its proof, asserting that it did not wish to sell the real estate but that it recognized the power and capacity of the Territory to condemn it. (R. 20.)

Judgment of condemnation was entered on December 1, 1937, and the court awarded $32,500, which it found to be the value of the land, as damages to petitioner. Later in the year 1937 petitioner received the price so fixed, and title to the land was vested in the Territory of Hawaii. (R. 20.)

The Commissioner treated the loss of $12,479.48, the difference between the adjusted cost basis of the land and the amount of the award, as resulting from the sale or exchange of a capital asset and therefore limited by Section 117 (d) of the Revenue Act of 1936 to $2,000 (R. 21). The Board of Tax Appeals sustained the Commisisoner's determination (R. 22–23), and the court below affirmed the Board (R. 40–41).

ARGUMENT

The decision of the court below is correct and presents no conflict.

Petitioner owned a capital asset which was transferred to another in return for a monetary consideration, pursuant to a condemnation proceeding. The fact that the transfer was involuntary does not alter the result that there was a sale of a capital asset. *Helvering* v. *Hammel,* 311 U. S. 504, 511. If there was a transfer of property rights which can properly be classed as a "sale or exchange" then the resulting loss was a capital loss, subject to the limitations prescribed by Section 117 (d) of the Revenue Act of 1936, *supra.* Since there was a transfer of property for a fixed price in money, the court below correctly held that there was a "sale" of the property within the meaning of that statute.

Petitioner, however, urges (Pet. 5) that the decision is probably in conflict with *Helvering* v. *Flaccus Leather Co.,* 313 U. S. 247. But in that

case the property was destroyed; it was not transferred to a new owner. The Court therefore held that there was not a "sale or exchange" under Section 117 (d). The instant case presents the problem of the *Hammel* case rather than that of the *Flaccus* case, for here, as in the *Hammel* case, there was a transfer of property to a new owner.[1]

The decision below is in accord with the result, uniformly reached by the lower courts, that gains or losses realized in condemnation proceedings are subject to the provisions of Section 117 (d). *Commissioner* v. *Kieselbach*, 127 F. (2d) 359, 360–361 (C. C. A. 3), pending on petition for certiorari in respect of other points, No. 184, this Term.[2]

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[1] In the *Flaccus* opinion the Court ruled that the result was unaffected by Section 112 (f) which merely provided for non-recognition of gains or loss on certain involuntary conversions of property. Section 112 (f) did not in any way deal with the question whether such gain or loss was to be classified as ordinary or capital. The Court did not rule that none of the involuntary conversions listed in Section 112 (f) could be classified as sales or exchanges under Section 117 (d); it simply ruled that Section 112 (f) had no bearing upon the classification of capital gains or losses under Section 117 (d).

[2] The issue, as far as here relevant, presented by the petition for certiorari in the *Kieselbach* case is whether the interest awarded in a condemnation proceeding is taxable as ordinary income or as capital gain. This also was the issue litigated in *Seaside Improvement Co.* v. *Commissioner*, 105 F. (2d) 990 (C. C. A. 2), certiorari denied, 308 U. S. 618; and in *Commissioner* v. *Appleby's Estate*, 123 F. (2d) 700 (C. C. A. 2). It appears to be implicit in these two cases that, whatever the taxability of the interest, the gain involved in the award itself is a capital gain and not ordinary income.

CONCLUSION

The decision below is correct and there is no conflict of authorities. The petition should be denied.

Respectfully submitted,

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